

Box 5

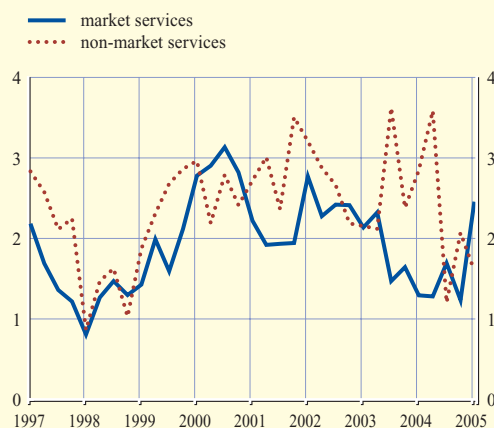
WHAT CAN EXPLAIN THE DIFFERENCES IN WAGE GROWTH BETWEEN MARKET AND NON-MARKET SERVICES?

Given the substantial weight of services in overall economic activity (nearly 70% of euro area value added), a clear understanding of wage developments in the services sector is crucial also for assessing inflationary pressures. In 2004 overall wage growth in the euro area services sector remained moderate, with an average annual growth rate of compensation per employee of 1.8%. However, this concealed significant differences within services. In particular, the annual growth rate of compensation per employee in “non-market” services (e.g. public administration, education, social security and health services, covering around 45% of total employment in services) was 2.4%, compared with 1.4% in more “market-oriented” services (e.g. trade, transport, finance and business services, accounting for around 55% of total employment in services). This difference also appears to have been persistent in recent years (see Chart A), although the differential widened between mid-2003 and mid-2004. Since 1997 the annual average growth rate of compensation per employee in “non-market” services, which are subject to less intense competitive pressures, has been on average 0.5 percentage point higher than in the more competitive market services. This Box analyses in more detail the reasons for differences in wage growth across different types of services.

Changes in part-time employment could partly explain recent patterns in services sub-sector wage growth. In total services, the proportion of part-timers rose from less than 18% to more than 22% between 1997 and 2004. Moreover the growth in part-time

Chart A Compensation per employee in services

(annual percentage changes)

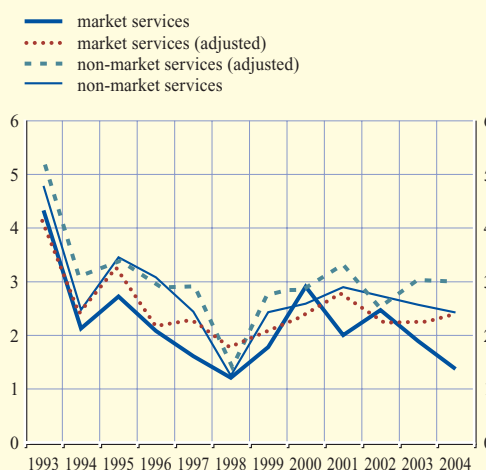


Sources: Eurostat and ECB calculations.

employment was stronger in market services (5.6% per year on average) than in the more “sheltered” services (3.1% per year on average). In 2004, the proportion of part-timers continued to rise in “market-oriented” services, but declined very slightly in the more sheltered services. Such developments have an impact on the overall wage structure since a higher proportion of part-time workers mechanically lowers the average number of hours worked and thus reduces average growth in compensation per employee. In addition, part-time employees tend to have lower hourly wages than full-time employees.¹ Using European Labour Force survey data on part-time work and average hours worked, it is possible to adjust the increase in wage growth for the impact of part-time work (see Chart B).²

Chart B Compensation per employee adjusted for part-time growth

(annual percentage changes)



Sources: Eurostat and ECB calculations.

Chart B confirms that, in 2004, developments in part-time work explain more than half of the gap in wage growth between the two sub-sectors of services. However, over the longer term, differences in the pattern of part-time employment do not explain the entire gap and why the annual growth rate of compensation per employee in more “sheltered” services was consistently higher than that of market services during the 1990s. Since 1997, after adjusting for the impact of part-time work, the average gap has been only marginally reduced to 0.4 percentage point on average.

Some other structural factors may be at play. In particular, average wage levels in the non-market services sector have been persistently below those in market services, despite the fact that more than a third of employees in non-market services are classified as highly skilled, compared with around 20% in market services.³ The persistence of the wage growth differential in recent years may thus also reflect a catching-up of average wage levels in non-market services.

Furthermore, the wage-setting process in a competitive sector may differ from that in more sheltered sectors. For example, the demand for and supply of services such as health, education and other public services, and hence labour demand and supply, may be partly determined by political processes that are not necessarily influenced by cyclical developments in the economy. In addition, the moderating impact of unemployment on wage claims may be lower in

1 See, for example, OECD Employment Outlook, June 1999.

2 The number of part-time employees may be converted to full-time equivalents, multiplying it by the ratio of “average hours worked by part-timers” to “average hours worked by full-timers”. This number is then added to the number of full-time employees to obtain total employees in full-time equivalents. Total compensation is then divided by the latter in order to estimate compensation per “full-time equivalent”.

3 See Genre, Momferatou and Mourre (2005), “Wage diversity in the euro area: an overview of labour cost differentials across industries”, ECB Occasional Paper No. 24, February.

less competitive services sectors. Indeed, the volatility of employment growth in sheltered services is significantly lower than in more competitive services.

Notwithstanding the above reasons for differences in wage growth within the services sector, the wage growth differential may also be the sign of some lack of efficiency or rigidities in some non-market services that could be addressed by policy measures. Furthering the necessary reform process across the euro area can thus be seen as a key determinant in shaping future wage growth trends in non-market services and thus in the economy as a whole.